



Financial Management Report as of JUNE 30, 2009

AT A GLANCE:

General Fund revenues continue to lag behind budget (page 3)

2009 Sales tax revenue \$1.5 million behind 2008 so far this year (page 5)

Where's the popcorn? (page 2 sidebar)

Have we hit bottom yet? (pages 7-8)

Inside this issue:

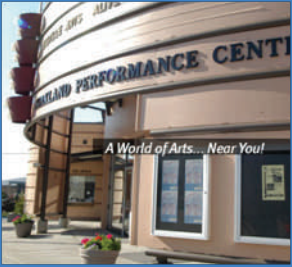
Expenditure Summary	2
General Fund Revenue	3
General Fund Expenditures	4
Sales Tax Revenue	5
Economic Environment	7
Investment Report	8
Reserve Summary	10

Summary of All Operating Funds: *Revenue*

- **General Fund** revenue is budgeted to increase 7.8 percent in 2009 over 2008, largely from increased business license fees, higher utility tax rates, and changes to internal charges. While actual 2009 revenue is **1.4 percent ahead** of the same period last year, it still lags behind budget due to significant declines in sales tax and development fee related revenue and disappointing utility tax and business license fee revenue. A more detailed analysis of overall General Fund revenue can be found on page 3 and sales tax revenue beginning on page 5.
- **Other General Government Funds** actual 2009 revenue is **3.5 percent ahead** of the same period last year due to higher internal rates and recreation revenue (partially due to an accounting change in 2009 that moved all recreation revenue to the Recreation Revolving Fund, as well as increased recreation class fees and participation. Lodging tax and motor vehicle fuel tax revenues are down 20.7 percent and 14.4 percent respectively compared to the same period last year. Motor vehicle fuel tax is collected on a flat rate per gallon, so increased fuel costs have a negative impact on this revenue. Even though fuel prices have dropped considerably, this revenue has not fully recovered.
- **Water Sewer Operating Fund** actual 2009 revenue is **1.7 percent behind** the same period last year due to slightly lower water revenue and a significant decrease in connection charge fee revenue (reflecting lower development-related activity) and despite moderate growth in sewer revenue. Water revenue trends may improve in coming months given the recent dry and warm weather.
- **Surface Water Management Fund** Surface Water fees are paid through property tax collection, which are primarily received in April and October. Actual 2009 revenue is essentially flat, **0.4 percent ahead** of the same period last year.
- **Solid Waste Fund** actual 2009 revenue is **1.3 percent ahead** of the same period last year, although it is slightly behind the budgeted amount.

Resources by Fund	Year-to-Date Actual			Budget			% of Budget	
	6/30/2008	6/30/2009	% Change	2008	2009	% Change	2008	2009
General Gov't Operating:								
General Fund	24,749,393	25,097,632	1.4%	53,895,913	58,081,118	7.8%	45.9%	43.2%
Other General Gov't Operating Funds	8,542,176	8,842,142	3.5%	16,562,562	16,902,757	2.1%	51.6%	52.3%
Total General Gov't Operating	33,291,569	33,939,774	1.9%	70,458,475	74,983,875	6.4%	47.2%	45.3%
Utilities:								
Water/Sewer Operating Fund	8,189,539	8,050,765	-1.7%	17,821,208	19,696,845	10.5%	46.0%	40.9%
Surface Water Management Fund	2,811,350	2,822,777	0.4%	5,274,145	5,231,700	-0.8%	53.3%	54.0%
Solid Waste Fund	4,235,031	4,290,974	1.3%	8,365,262	8,612,724	3.0%	50.6%	49.8%
Total Utilities	15,235,919	15,164,515	-0.5%	31,460,615	33,541,269	6.6%	48.4%	45.2%
Total All Operating Funds	48,527,488	49,104,290	1.2%	101,919,090	108,525,144	6.5%	47.6%	45.2%

Budgeted and actual revenues exclude resources forward and interfund transfers.



Sundance, Tribeca, Cannes, Kirkland?

Kirkland was selected as a venue for the Seattle International Film Festival (SIFF), which ran from May 21 to June 14. SIFF is the largest film festival (measured by number of films) in the country with 160,000 attendees viewing over 300 independent and foreign films and documentaries. The screenings in Kirkland were held at the Kirkland Performance Center and a first for SIFF—outdoor screenings at Juanita Beach Park.



A "victory garden" has been temporarily located on city-owned vacant property adjacent to City Hall. Historically these gardens were common during World War II to supplement food rationing. The project is supported by donations and volunteer labor from City employees on their own time and their family and friends. The produce will be donated to the local food bank, Hopelink.

Information about starting your own victory garden is available at <http://www.revivevictorygarden.org/>

Summary of All Operating Funds: *Expenditures*

- **General Fund** actual expenditures are **8.1 percent ahead** of last year primarily due to higher personnel costs, payments for the new regional dispatch agency, and accounting changes that moved all recreation expenditures to the General Fund and increased internal charges for Facilities (see the explanation of the accounting changes in the box below).
- **Other Operating Funds** actual expenditures are **9 percent behind** the same period last year due to lower fuel costs, timing of vehicle and computer purchases, the previously mentioned accounting change for Recreation Revolving fund expenditures and despite higher personnel costs.
- **Water/Sewer Operating Fund** actual expenditures are **3.7 percent ahead** of the same period last year due to higher water purchase costs and METRO sewer costs and despite a significant decline in regional water connection charges.
- **Surface Water Management Fund** actual expenditures are **14.4 percent ahead** of the same period last year due higher personnel costs and internal rates.
- **Solid Waste Fund** actual expenditures are **2.4 percent behind** the same period last year due to the normal variability of collection and timing of disposal contract billing and tax payments.

- *An accounting change for the Recreation Revolving Fund occurred in 2009. The fund is now used to account for all parks and recreation-related revenue. All expenditures related to parks and recreation programs are consolidated in the General Fund. A periodic interfund transfer is budgeted from the Recreation Revolving Fund to the General Fund. The purpose of the accounting change was to better identify the General Fund subsidy of recreation programs and functions.*
- *Facilities charges (an internal service charge) for General Fund departments were increased as a result of an accounting change. In previous years, cable and admissions taxes were allocated directly to the Facilities Fund, which in effect subsidized the rate charged to General Fund departments. Beginning in 2009, these revenues are directly allocated to the General Fund. The resulting increase to the internal rates charged to the General Fund is covered by the revenue shift.*

Expenditures by Fund	Year-to-Date Actual			Budget			% of Budget	
	6/30/2008	6/30/2009	% Change	2008	2009	% Change	2008	2009
General Gov't Operating:								
General Fund	27,363,253	29,578,885	8.1%	56,150,641	59,198,012	5.4%	48.7%	50.0%
Other General Gov't Operating Funds	7,600,028	6,915,925	-9.0%	15,817,164	15,665,192	-1.0%	48.0%	44.1%
Total General Gov't Operating	34,963,281	36,494,810	4.4%	71,967,805	74,863,204	4.0%	48.6%	48.7%
Utilities:								
Water/Sewer Operating Fund	6,878,829	7,133,030	3.7%	13,718,748	15,589,932	13.6%	50.1%	45.8%
Surface Water Management Fund	1,337,604	1,530,864	14.4%	2,695,982	3,405,833	26.3%	49.6%	44.9%
Solid Waste Fund	3,582,247	3,497,890	-2.4%	8,221,762	8,429,227	2.5%	43.6%	41.5%
Total Utilities	11,798,680	12,161,784	3.1%	24,636,492	27,424,992	11.3%	47.9%	44.3%
Total All Operating Funds	46,761,961	48,656,594	4.1%	96,604,297	102,288,196	5.9%	48.4%	47.6%

Budgeted and actual expenditures exclude working capital, operating reserves, capital reserves, and interfund transfers.

General Fund Revenue

The City adopted a \$2.6 million budget reduction in July for 2009 sales tax revenue in response to the significant revenue shortfall. This budget adjustment will be reflected in the September report.

- **Sales tax** revenue allocated to the General Fund for 2009 was budgeted to decrease by 9.4 percent from the 2008 budget, more closely reflecting actual 2008 receipts. However, actual General Fund revenue is **down 18.8 percent** compared to the same period last year (note that a portion of the tax allocated to capital improvement plan projects in 2008 was moved to the General Fund in 2009). A detailed analysis of **sales tax** revenue can be found beginning on page 5.
- **Utility tax** 2009 revenue was budgeted to increase 35.6 percent over 2008 due to higher utility tax rates and the shift of cable tax revenue from the Facilities Fund. Actual revenue collection is only **12.3 percent ahead** of the same period last year primarily due to the shift of cable tax; otherwise revenue would be up about 3 percent. Utility tax rates were increased for water, sewer, and garbage in 2009; however, they are lagging behind budget partially due to timing of receiving revenue at that higher tax rate. Telephone utility tax is 14.3 percent behind the same period last year possibly reflecting consumer response to the economic downturn and the results of a change in federal regulations in mid-2008. Revised revenue estimates project a shortfall of about \$0.5 million from budget in 2009.
- **Other taxes** actual revenue is **13.3 percent behind** the same period last year primarily due to the one-time receipt of E-911 tax revenue in 2008 for reimbursement of dispatch expenses (a 2009 reimbursement is expected in September) and despite the shift of admissions tax from the Facilities Fund.
- While **business licenses** (base fee) and **franchise fees** actual revenue is **2.3 percent behind** the same period last year, the **revenue generating regulatory license fee** is **101.1 percent ahead** of the same period last year due to a significant rate increase. However, this revenue is also lagging behind budget, which reflects the new fee structure; revised estimates project a 2009 budget shortfall of about \$0.2 million.
- The current recession is reflected in **development-related fee** revenues, which collectively are **down 26.7 percent** compared to the same period in 2008. **Plan check** revenue is **62.2 percent lower**, **planning fees** are **43.8 percent lower**, and **engineering services** revenue is **28.6 percent lower**. **Building permit** revenue is **5.5 ahead** primarily due to permits issued for a large school replacement project and two large mixed-used projects and despite the significant decline in single family permits.
- Compared to the same period last year: **Grant** revenue is **significantly ahead** partly due to funding received for the environmental outreach program; **State shared revenues** are **40.5 percent ahead** due to mitigation revenue received for the loss of sales tax revenue resulting from streamlined sales tax sourcing rule changes;
- **Internal Charges** are **27.6 percent ahead** compared to the same period last year due to increased capital project engineering charges, as well as higher internal service costs allocated to other operating funds.

General Fund 2009 revenues are \$0.35 million higher than the same period in 2008 largely due to utility tax, revenue generating regulatory license revenue and internal charges and despite significantly lower sales tax and development-related revenue. Overall, revenue is lagging behind budget; as a result the City is making mid-year expenditure adjustments.

The General Fund is the largest of the General Government Operating funds. It is primarily tax supported and accounts for basic services such as public safety, parks and recreation, and community development.

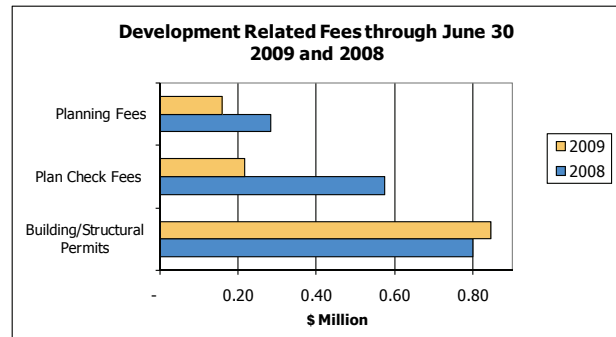
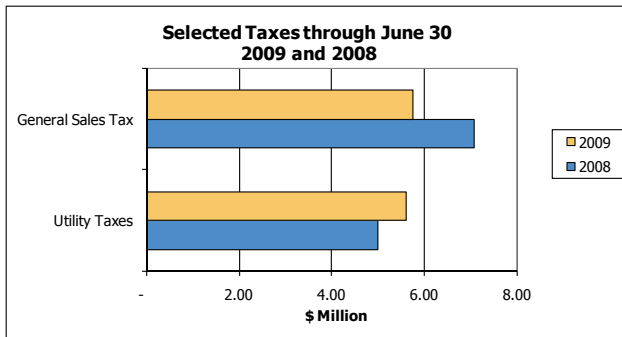
About 378 of the City's 476 regular employees are budgeted within this fund.

General Fund Resource Category	Year-to-Date Actual						% of Budget	
	6/30/2008	6/30/2009	% Change	2008	2009	% Change	2008	2009
Taxes:								
Retail Sales Tax: General	7,068,768	5,739,725	-18.8%	15,756,800	14,280,801	-9.4%	44.9%	40.2%
Retail Sales Tax: Criminal Justice	569,086	483,289	-15.1%	1,050,000	1,107,000	5.4%	54.2%	43.7%
Property Tax	4,825,375	4,858,805	0.7%	9,037,710	9,264,941	2.5%	53.4%	52.4%
Utility Taxes	4,985,699	5,596,810	12.3%	8,546,130	11,586,963	35.6%	58.3%	48.3%
Rev Generating Regulatory License	566,150	1,138,323	101.1%	990,000	2,654,920	168.2%	57.2%	42.9%
Other Taxes	244,678	212,209	-13.3%	664,713	658,900	-0.9%	36.8%	32.2%
Total Taxes	18,259,756	18,029,162	-1.3%	36,045,353	39,553,525	9.7%	50.7%	45.6%
Licenses & Permits:								
Building, Structural & Equipment Permits	800,081	843,820	5.5%	2,163,450	1,679,600	-22.4%	37.0%	50.2%
Business Licenses/Franchise Fees	792,595	774,490	-2.3%	1,449,450	1,673,471	15.5%	54.7%	46.3%
Other Licenses & Permits	157,528	100,476	-36.2%	193,900	190,000	-2.0%	81.2%	52.9%
Total Licenses & Permits	1,750,205	1,718,786	-1.8%	3,806,800	3,543,071	-6.9%	46.0%	48.5%
Intergovernmental:								
Grants	102,002	184,435	80.8%	155,260	175,675	13.1%	65.7%	105.0%
State Shared Revenues & Entitlements	318,224	446,999	40.5%	645,318	681,104	5.5%	49.3%	65.6%
Fire District #41	-	30,694	N/A	3,487,428	3,754,077	N/A	N/A	0.8%
EMS	-	-	N/A	793,023	836,938	N/A	N/A	N/A
Other Intergovernmental Services	311,030	452,961	45.6%	439,609	480,103	9.2%	70.8%	94.3%
Total Intergovernmental	731,256	1,115,089	52.5%	5,520,638	5,927,897	7.4%	13.2%	18.8%
Charges for Services:								
Internal Charges	1,679,161	2,143,083	27.6%	3,511,012	4,344,629	23.7%	47.8%	49.3%
Engineering Services	324,212	231,520	-28.6%	610,000	570,000	-6.6%	53.1%	40.6%
Plan Check Fee	572,904	216,733	-62.2%	900,000	750,000	-16.7%	63.7%	28.9%
Planning Fees	282,675	158,989	-43.8%	1,194,637	373,673	-68.7%	23.7%	42.5%
Recreation*	40,511	-	-100.0%	83,000	-	-100.0%	48.8%	N/A
Other Charges for Services	313,057	410,243	31.0%	688,323	914,594	32.9%	45.5%	44.9%
Total Charges for Services	3,212,521	3,160,569	-1.6%	6,986,972	6,952,896	-0.5%	46.0%	45.5%
Fines & Forfeits	589,744	644,549	9.3%	1,132,000	1,435,000	26.8%	52.1%	44.9%
Miscellaneous	205,911	429,478	108.6%	404,150	668,729	65.5%	50.9%	64.2%
Total Revenues	24,749,393	25,097,632	1.4%	53,895,913	58,081,118	7.8%	45.9%	43.2%
Other Financing Sources:								
Interfund Transfers	28,838	476,143	N/A	1,441,253	1,740,650	N/A	2.0%	27.4%
Total Other Financing Sources	28,838	476,143	N/A	1,441,253	1,740,650	N/A	2.0%	27.4%
Total Resources	24,778,231	25,573,775	3.2%	55,337,166	59,821,768	8.1%	44.8%	42.7%

Budgeted and actual revenues exclude resources forward.

*2009 Recreation revenue is accounted for in the Recreation Revolving Fund; see accounting note on page 2.

General Fund Revenue *continued*



General Fund Expenditures

General Fund Department Expenditures	Year-to-Date Actual			Budget			% of Budget	
	6/30/2008	6/30/2009	% Change	2008	2009	% Change	2008	2009
Non-Departmental	501,809	549,417	9.5%	1,391,813	1,134,474	-18.5%	36.1%	48.4%
City Council	229,800	213,198	-7.2%	362,034	347,972	-3.9%	63.5%	61.3%
City Manager's Office	1,829,955	1,690,813	-7.6%	3,784,425	3,383,703	-10.6%	48.4%	50.0%
Human Resources	514,409	520,556	1.2%	1,122,706	1,087,358	-3.1%	45.8%	47.9%
City Attorney's Office	463,776	506,946	9.3%	991,985	994,817	0.3%	46.8%	51.0%
Parks & Community Services	2,656,723	3,155,091	18.8%	6,059,645	7,543,480	24.5%	43.8%	41.8%
Public Works (Engineering)	1,700,269	1,726,429	1.5%	3,578,878	3,802,468	6.2%	47.5%	45.4%
Finance and Administration	1,708,415	1,842,366	7.8%	3,536,915	3,632,588	2.7%	48.3%	50.7%
Planning & Community Development	1,735,650	1,414,716	-18.5%	3,381,197	2,895,782	-14.4%	51.3%	48.9%
Police	7,660,269	8,749,359	14.2%	15,021,285	16,673,163	11.0%	51.0%	52.5%
Fire & Building	8,362,178	9,209,994	10.1%	16,919,758	17,702,207	4.6%	49.4%	52.0%
Total Expenditures	27,363,253	29,578,885	8.1%	56,150,641	59,198,012	5.4%	48.7%	50.0%
Other Financing Uses:								
Interfund Transfers	243,063	378,762	55.8%	1,593,416	1,799,441	12.9%	15.3%	21.0%
Total Other Financing Uses	243,063	378,762	55.8%	1,593,416	1,799,441	12.9%	15.3%	21.0%
Total Expenditures & Other Uses	27,606,316	29,957,647	8.5%	57,744,057	60,997,453	5.6%	47.8%	49.1%

Budgeted and actual expenditures exclude working capital, operating reserves, and capital reserves.

Facilities charges (an internal service charge) for General Fund departments were increased as a result of an accounting change. In previous years, cable and admissions taxes were allocated directly to the Facilities Fund, which in effect subsidized the rate charged to General Fund departments. Beginning in 2009, these revenues are directly allocated to the General Fund. The resulting increase to the internal rate charged to the General Fund is covered by the revenue shift.

Comparing to the same period last year:

- Actual 2009 expenditures for **Non-Departmental** are **9.5 percent ahead** primarily due to higher retiree medical costs and internal professional services.
- Actual 2009 expenditures for the **City Council** are **7.2 percent lower** primarily due to the one-time cost of a citizen survey in 2008 and the expenditure reduction eliminating meals for Council meetings, yet despite increased internal service charges and higher dues and membership costs.
- Actual 2009 expenditures for the **City Manager's Office** are **7.6 percent lower** due to one-time charges incurred last year for setting up a regional dispatch agency, and despite higher personnel costs and internal service charges. As of 2009, ongoing expenses for the regional dispatch agency are budgeted in the Police and Fire departments.
- Actual 2009 expenditures for the **City Attorney's Office** are **9.3 percent ahead** due to higher personnel costs, outside legal services, and internal service charges.
- Actual 2009 expenditures for the **Parks & Community Services Department** are **18.8 percent ahead** primarily due to higher personnel costs and internal service charges, as well as the accounting change moving all recreation program expenses to the General Fund (see explanation on page 2). Note that the increase is less than budgeted.

Compared to 2008 2009 General Fund actual expenditures are 8.1 percent higher primarily due to increased internal service rates as noted to the left and higher personnel costs.

(Continued on page 5)

Financial Management Report as of JUNE 30, 2009

- Actual 2009 expenditures for the **Finance and Administration Department** are **7.8 percent ahead** due to higher personnel costs, internal service charges and election costs, which were higher than normal due to the presidential election.
- Actual 2009 expenditures for the **Planning and Community Development Department** are **18.5 percent lower** due to the shift of regional housing funding to another fund, one-time projects that were underway in 2008 and reduced personnel costs due to reductions in staff.
- Actual 2009 expenditures for the **Police Department** are **14.2 percent ahead** due to charges for the regional dispatch agency and higher internal charges. Kirkland dispatch staff were relocated to the new agency as of July 1st. Higher jail costs were a concern in 2008 when actual expenses were almost at budget by June; expenses in 2009 are down about 8.9 percent from last year but tracking slightly ahead of budget.
- Actual 2009 expenditures for the **Fire & Building Department** are **10.1 percent ahead** due to higher personnel costs and internal service charges. Fire suppression overtime remains a concern; while 2009 expenses are down almost 12 percent from last year, they are still tracking higher than planned due to an unexpected increase in the number of disabilities experienced this year and despite the four additional firefighters starting in April to help reduce this expense.

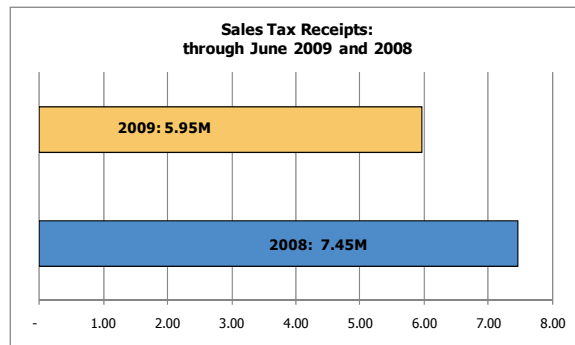


The 2009-10 City of Kirkland Budget document earned the "Distinguished Budget Presentation Award" from the Government Finance Officers Association for the twelfth consecutive time.

Sales Tax Revenue Analysis Total 2009 actual revenue is **down 20.2 percent** compared to the same period last year, which translates to over \$1.5 million reduction in revenue. This is a continuation of the generally negative trend that started in the third quarter of 2007. Primary factors include significant decline in contracting revenue, as well as reduced revenue in all retail sectors. All business sectors continue to experience negative performance compared to the same period last year (see table on page 6).

Review by business sectors:

- The **contracting** sector is **31 percent down** compared to the same period last year due to the completion of major projects and the significant decline of development activity in response to the current recession.
- Auto/gas retail** is **23.4 percent down** compared to the same period last year due to disappointing performance by most retailers and the temporary closure of two dealerships for about two months. Local trends reflect the trends experienced nationally in this sector.
- Wholesale** is **40.2 percent down** compared to the same period last year primarily due to a reduction in development-related activity and also due to changes in local coding sourcing rules from streamlined sales tax.
- Other retail** is **15.6 percent down** compared to the same period last year due to generally negative performance in most retail sectors included in this group, especially building materials and electronic equipment.
- General merchandise/miscellaneous retail** is **11 percent down** compared to the same period last year due to disappointing performance by key retailers reflecting reduced consumer spending in response to the recession. This sector has also been impacted by streamlined sales tax sourcing rule changes.
- The **miscellaneous** sector is **20.1 percent down** compared to the same period last year due to slumping finance/insurance and real estate sectors.
- Retail eating/drinking** is **14.6 percent down** compared to the same period last year. This sector continues its negative trend that started in the second half of 2008 as consumers reduced discretionary spending in response to economic conditions.
- The **services** sector is **8.1 percent down** compared to the same period last year largely due to declines in software, car/equipment leasing and accommodations. The accommodations sector continued negative performance for the sixth month in a row, down 16.2 percent compared to the same period last year.
- The **communications** sector is **16.2 percent down** compared to the same period last year due to changes in levels of development-related activity as well as reduced consumer spending for telecommunications services.



Streamlined Sales Tax

Washington State implemented new local coding sales tax rules as of July 1, 2008 as a result of joining the national Streamlined Sales Tax Agreement. Any negative impact from this change is mitigated by the State of Washington. Kirkland received mitigation payment checks for \$75,000 in December, \$77,000 in March, and \$45,000 in June.

Neighboring Cities

2009 sales tax revenue for Bellevue is down 20.6 percent and Redmond is down 4.4 percent through June compared to the same period in 2008.

City of Kirkland Actual Sales Tax Receipts

Business Sector Group	January-June		Dollar Change	Percent Change	Percent of Total	
	2008	2009			2008	2009
Services	800,410	735,281	(65,129)	-8.1%	10.7%	12.4%
Contracting	1,234,687	851,829	(382,858)	-31.0%	16.6%	14.3%
Communications	284,874	238,677	(46,197)	-16.2%	3.8%	4.0%
Auto/Gas Retail	1,558,087	1,192,923	(365,164)	-23.4%	20.9%	20.1%
Gen Merch/Misc Retail	1,097,670	976,868	(120,802)	-11.0%	14.7%	16.4%
Retail Eating/Drinking	634,570	542,165	(92,405)	-14.6%	8.5%	9.1%
Other Retail	879,219	741,966	(137,253)	-15.6%	11.8%	12.5%
Wholesale	498,702	298,014	(200,688)	-40.2%	6.7%	5.0%
Miscellaneous	465,442	371,997	(93,445)	-20.1%	6.2%	6.3%
Total	7,453,661	5,949,720	(1,503,941)	-20.2%	100.0%	100.0%

Kirkland's sales tax base is comprised of a variety of businesses which are grouped and analyzed by business sector (according to NAICS, or "North American Industry Classification System"). Nine business sector groupings are used to compare 2008 and 2009 year-to-date sales tax receipts in the table to the left.

Month	Sales Tax Receipts		Dollar Change	Percent Change
	2008	2009		
January	1,227,855	994,146	(233,709)	-19.0%
February	1,586,493	1,224,935	(361,558)	-22.8%
March	1,112,704	954,492	(158,212)	-14.2%
April	1,085,739	867,726	(218,013)	-20.1%
May	1,367,777	1,007,790	(359,987)	-26.3%
June	1,073,093	900,631	(172,462)	-16.1%
Total	7,453,661	5,949,720	(1,503,941)	-20.2%

When analyzing monthly sales tax receipts, there are two items of special note: First, most businesses remit their sales tax collections to the Washington State Department of Revenue on a monthly basis. Small businesses only have to remit their sales tax collections either quarterly or annually, which can create anomalies when comparing the same month between two years. Second, for those businesses which remit sales tax monthly, there is a two month lag from the time that sales tax is collected to the time it is distributed to the City. For example, sales tax received by the City in June is for sales activity in April. Monthly sales tax receipts through June 2008 and 2009 are compared in the table to the left.

- Negative monthly comparison trends, with the exception of February 2008, have been occurring since July 2007.
- Sourcing rule changes were adopted as of July 1, 2008 as a result of streamlined sales tax legislation. Mitigation payments from Washington State have been received, which help offset the impact of revenue lost due to the rule changes. Factoring in these payments would change the decline between 2009 and 2008 to about 17.5 percent.
- A key retailer double-posted payments in May 2008, which was corrected in June. Normalizing for this correction changes May to 20.9 percent behind and June to 22.5 percent behind the same months in 2008.

Kirkland's sales tax base is further broken down by business district (according to geographic area), as well as "unassigned or no district" for small businesses and businesses with no physical presence in Kirkland.

Comparing to the same period last year:

Totem Lake, which accounts for almost 31 percent of the total sales tax receipts, is **24.2 percent down** primarily

due to slumping automotive/gas retail sales and generally weak retail and finance/real estate activity. Almost 63 percent of this business district's revenue comes from the auto/gas retail and general merchandise/miscellaneous retail sectors.

NE 85th Street, which accounts for 16 percent of the total sales tax receipts, is **13.7 percent down** primarily due to the general merchandise/miscellaneous retail and automotive/gas retail sectors, which contribute 85 percent of this business district's revenue.

Downtown, which accounts for 7.5 percent of the total sales tax receipts, is **19.3 percent down** due to the loss of several small retailers and poor performance in the retail eating/drinking and accommodations sectors; these sectors

provide over 68 percent of this business district's revenue.

Houghton and Bridle Trails, which collectively account for about 3 percent of the total sales tax receipts, are **32 percent down** almost entirely due to miscellaneous retail and other retail, which provides over 50 percent of these business districts' revenue.

Carillon Point/Yarrow Bay, which accounts for over 2 percent of the total sales tax receipts, is **32.8 percent down** compared to last year primarily due to poor performance from major software companies, retail eating/drinking and the accommodations sectors. Almost 75 percent of this business district's revenue comes from retail eating/drinking, hotels, and banking services.

Juanita, which accounts for over 2 percent of the total sales tax receipts, is **13.8 percent down** primarily due to retail eating/drinking. A one-time recovery received in 2008 in this sector skews comparisons between the years. Normalizing for this event, this business district would be down about 6 percent. Retail eating/drinking and business and personal services provide almost 45 percent of this business district's revenue.

When reviewing sales tax receipts by business district, it's important to point out that over 40 percent of the revenue received in 2009 is in the "unassigned or no district" category largely due to contracting revenue and revenue from Internet, catalog sales and other businesses located outside of the City. While these sectors' revenue are down from 2008; their share of total revenue increased from 38.8 percent to 40.3 percent.

City of Kirkland Sales Tax by Business District

Business District	Jan - Jun Receipts		Dollar Change	Percent Change	Percent of Total	
	2008	2009			2008	2009
Totem Lake	2,410,364	1,827,588	(582,776)	-24.2%	32.3%	30.7%
NE 85th St	1,103,074	951,895	(151,179)	-13.7%	14.8%	16.0%
Downtown	556,041	448,631	(107,410)	-19.3%	7.5%	7.5%
Carillon Pt/Yarrow Bay	215,121	144,533	(70,588)	-32.8%	2.9%	2.4%
Houghton & Bridle Trails	274,629	186,736	(87,893)	-32.0%	3.7%	3.1%
Juanita	157,950	136,140	(21,810)	-13.8%	2.1%	2.3%
Unassigned or No District:						
Contracting	1,234,687	851,829	(382,858)	-31.0%	16.6%	14.3%
Other	1,501,795	1,402,368	(99,427)	-6.6%	22.2%	26.0%
Total	7,453,661	5,949,720	(1,503,941)	-20.2%	100.0%	100.0%

Sales Tax Revenue Outlook Sales tax performance for the first half of 2009 is consistent with the negative trend experienced since the second half of 2007 primarily due to significant declines in development-related activities as well as the automobile/gas retail sector. Local consumer spending remains weak in all retail sectors. The loss of one major retailer will impact sales tax revenue for the second half of the year, which is better than the previous news when it appeared that Costco Home was closing as well (it remains open under new ownership). Declining development activity as a result of both the completion of major projects and continuing economic uncertainty impacts sales tax revenue not only in the contracting sector, but also wholesale, services, and communications sectors. Two large projects have or will start soon, and government incentives and aggressive discounting by auto dealers may help turn these key sectors around as the year progresses. The uncertain economic times dampens consumer discretionary spending, which impacts several of the City's sales tax producers including auto dealers and restaurants.

OFFICE VACANCIES:

According to CB Richard Ellis Real Estate Services, the Eastside vacancy rate is 14.2 percent for second quarter 2009 compared to 10.1 percent for second quarter 2008. Kirkland's 2009 rate is 17.2 percent, significantly higher than the 2008 rate of 3.8 percent.

- Over 1.8 million square feet of new construction office space came on the market in the Puget Sound region recently; about two thirds pre-leased and the rest vacant. Microsoft is occupying over 1.1 million square feet at the new Bravern complex in Bellevue.
- New leasing activity in the region is very slow. Landlords are concerned that vacant space will remain vacant for a long time, which will depress lease rates.
- In Kirkland, Google recently resumed its move into at least one of the three new office buildings.

LODGING TAX REVENUE:

Lodging tax 2009 revenue is down 20.7 percent compared to the same period last year as a result of the recession.

Economic Environment Update It appears that the worst of the "Great Recession" may be over. Both nationally and in Washington State, economic activity continues to decline, but at a slower pace. Most measures of economic activity have already or will soon bottom out. Credit conditions have eased significantly since the freeze experienced last fall. Most economists predict a slow "U-shaped" recovery following a turning point in the third quarter of this year. This opinion is not unanimous; see the economic outlook remarks in the investment section on page 9 sidebar. While Washington State entered the recession later than the rest of the nation, it is expected to emerge about the same time and with stronger growth. However, even with these hopeful signs, the June report released by the Washington State Economic and Revenue Forecast Council forecasts state revenues for the 2009-11 biennium at \$297 million less than the March forecast and notes that the new forecast includes \$226 million in new revenue as a result of legislation.

King County's unemployment rate has more than doubled in the last year, from 4.2 percent in June 2008 to 8.8 percent in June 2009. This is still below the national and state rate of 9.5 percent and 9.2 percent respectively. Conway Pedersen Economics predicts 2009 will see a 3.4 percent reduction in employment in 2009 and a loss of 0.7 percent in 2010 in the Puget Sound region.

Various confidence indices send mixed signals. The Western Washington Chapter of Purchasing Managers June survey index rose 2 points from May to 48.5. The national index also rose two points to 44.8. An index reading greater than 50 indicates a growing economy, while scores below suggest a shrinking economy. However, the Puget Sound Journal Business Confidence Index June survey of local executives conducted by Hebert Research reached its lowest mark in nearly a decade at 28. In comparison, the historical mean for the index is 54.79. Consumer confidence slipped unexpectedly in June to 49.3 from 54.8 in May, reflecting concerns about job loss and rising energy costs.

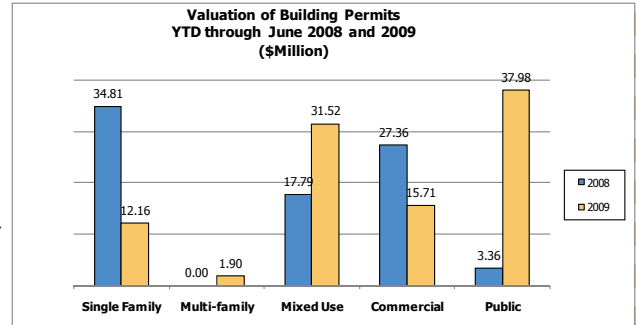
Seven of the Conference Board index's 10 "leading" indicators rose in June, including building permits, stock prices, manufacturers' new orders for consumer goods and positive readings on jobs. Consumer expectations, manufacturers' orders for capital goods and the real money supply weighed down the forecast. The index rose 0.7 percent from the prior month.

(Continued on page 8)

Local **development activity** through June comparing 2009 to 2008, as measured by the valuation of City of Kirkland building permits, is illustrated in the chart to the right. Activity dropped considerably in the single family sector. However, a spike in mixed-use permits from two large projects along with public sector activity offsets some of the declines elsewhere. Overall building and development permit and fee revenues are down 26.7 percent from 2008 levels.

King County June home sales were the highest since October 2007. Pending sales of **new and existing single-family homes** on the Eastside edged up 3.9 percent in June 2009 compared with a year earlier. However, the median price of a single family home declined 14.1 percent from June 2008 (\$538,000 compared to \$626,500). Condominium sales were down 19.1 percent and median prices fell 14.8 percent from the prior year (\$260,000 compared to \$305,000). Nationally, sales of existing homes rose for the fifth consecutive month in June. Median prices also increased for the fourth consecutive month, but are still down 16.7 percent from the high in June 2007.

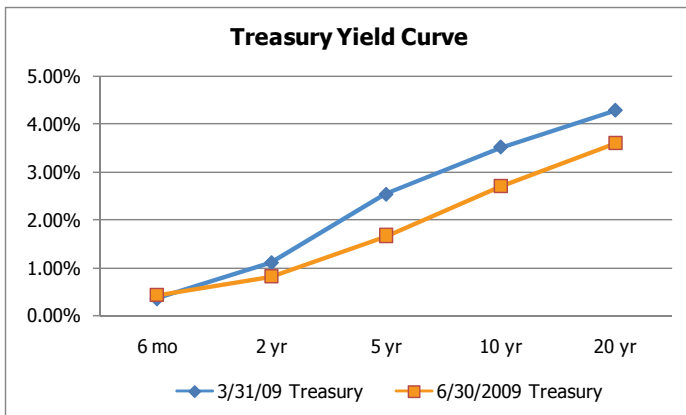
Seattle metro 2008 CPI, consistent with the national index, was volatile throughout last year. Seattle peaked at 6.19 percent in June and August, but dropped to 1.1 percent in December and ended 2008 with an average annual rate of 4.5 percent. The national index peaked at 6.2 percent in July and ended the year with an average annual rate of 4.1 percent. The June 2009 CPI was negative for the first time in several years, -0.7 percent. This index point is used for calculating City employee cost of living adjustments for 2010. Most of the bargaining units had already agreed to take no increase prior to the index announcement to help solve the City's current revenue shortfall. The national June CPI was also negative, -2.0 percent.



Investment Report

MARKET OVERVIEW

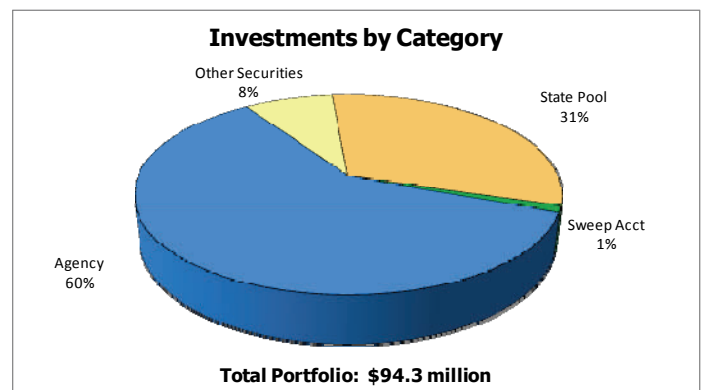
The Fed Funds rate continued at zero to 0.25 percent. The decline in the economy has slowed but continues its trend downward. The yield curve became steeper at the long end of the curve while the short end of the curve remained the same. The Treasury rates for 2 years and greater increased during the 2nd quarter.



Typically, the portfolio increases during the 2nd quarter due to the first half of the year property tax payments. However, this quarter, the Municipal Court building was purchased for \$2.7 million, the decline in revenues is beginning to be seen in the size of the portfolio and the Fire District payment for the first half of 2009 (\$1.8 million) arrived after the end of the quarter.

Diversification

The City's current investment portfolio is composed of Government Agency bonds, State and Local Government bonds, the State Investment Pool and an overnight bank sweep account. City investment procedures allow for 100 percent of the portfolio to be invested in U.S. Treasury or Federal Government obligations.



CITY PORTFOLIO

The primary objectives for the City of Kirkland's investment activities are: legality, safety, liquidity and yield. Additionally, the City diversifies its investments according to established maximum allowable exposure limits so that reliance on any one issuer will not place an undue financial burden on the City.

The City's portfolio decreased in the 2nd quarter of 2009 to \$94.3 million compared to \$97.4 million on March 31, 2009.

2009 ECONOMIC OUTLOOK and INVESTMENT STRATEGY

The economy looks weaker now than it did in February, according to 51 forecasters surveyed by the Federal Reserve Bank of Philadelphia. GDP growth for 2009 is expected to be negative 2.8 percent and core inflation to be 1.3 percent. The forecasters continue to see little threat of accelerating inflation. The unemployment rate is expected to average 9.1 percent in 2009. The Fed Funds rate, currently at 0.25 percent, is expected to remain at this level through the 1st quarter of 2010.

The duration of the portfolio will continue decreasing as securities mature and are called. New security purchases will be made as opportunities to obtain moderate returns become available. The objective during periods of low interest rates is to keep the portfolio duration shorter, with greater liquidity, so that the City is in a position to purchase securities with higher returns when interest rates begin to rise. The State Pool is currently near 0.60 percent and will continue to decline as the Fed Funds rate remains at .25 percent. Total estimated investment income for 2009 is \$2.8 million.

Investment Report *continued*

Liquidity

The target duration for the City's portfolio is based on the 2 year Treasury rate which increased from .81 percent on March 31, 2009 to 1.11 percent on June 30, 2009. The average maturity of the City's investment portfolio decreased

from 2.25 years on March 31, 2009 to 1.81 years on June 30, 2009 due to higher yielding securities being called on their call dates. It is expected that the higher yielding securities will continue to be called on their call dates as the interest rates of the securities are higher than current rates.

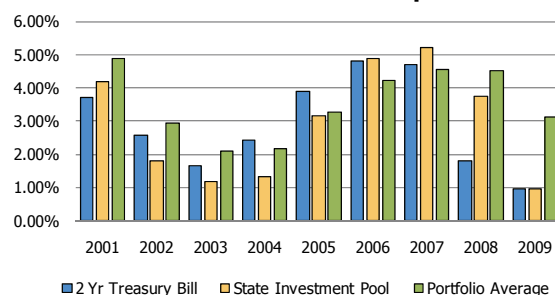
Yield

The City portfolio yield to maturity decreased from 3.30 percent on March 31, 2009 to 2.84 percent on June 30, 2009. Through June 30, 2009, the City's annual average yield to maturity was 3.12 percent. The City's portfolio outperformed the State Investment Pool annual average yield to maturity of 0.94 percent and the 2 Year Treasury Note annual average for 2009 of 0.95 percent due to the rapid decline in interest rates.

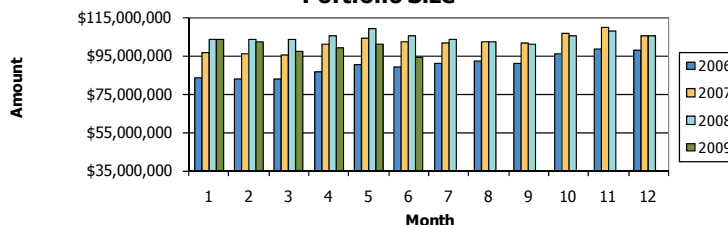
The City's practice of investing further out on the yield curve than the State Investment Pool results in earnings higher than the State Pool during declining interest rates and lower earnings than the State Pool during periods of rising interest rates. This can be seen in the adjacent graph.

Benchmark Comparison	March 31, 2009	June 30, 2009
City Yield to Maturity (YTM)	3.30%	2.84%
City Average YTM	3.30%	3.12%
City Year to Date Yield	3.29%	3.29%
State Pool Average Yield	1.12%	0.94%
2 yr Treasury Note Avg YTM	0.92%	0.95%

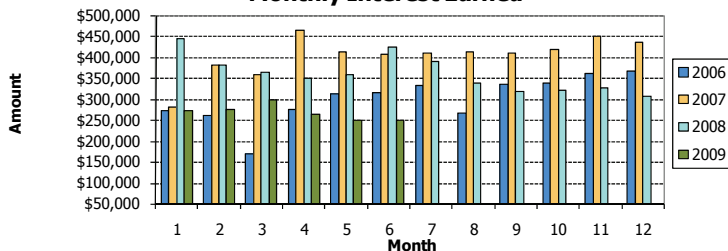
Investment Interest Rate Comparisons



Portfolio Size



Monthly Interest Earned



Reserve Summary

General Operating Reserve

For the City's "Rainy Day" fund, the target is established by fiscal policy at five percent of the operating budget (excluding utility and internal service funds). Each year, the target amount will change proportional to the change in the operating budget. To maintain full funding, the increment between five percent of the previous year's budget and the current budget would be added or subtracted utilizing interest income and year-end transfers from the General Fund. It is a reserve to be used for unforeseen revenue losses and other temporary events. If the reserve is utilized by the City Council, the authorization should be accompanied by a plan for replenishing the reserve within a two to three year period.

Revenue Stabilization Reserve

The Revenue Stabilization Reserve was approved by Council in July 2003 and was created by segregating a portion of the General Operating Reserve. The purpose of this reserve is to provide an easy mechanism to tap reserves to address temporary revenue shortfalls resulting from temporary circumstances (e.g. economic cycles, weather-related fluctuations in revenue). Council set the target at ten percent of selected General Fund revenue sources which are subject to volatility (e.g. sales tax, development fees and utility taxes). The Revenue Stabilization Reserve may be used in its entirety; however, replenishing the reserve will constitute the first priority for use of year-end transfers from the General Fund.

Contingency Fund

The Contingency Fund was established pursuant to RCW 35A.33.145 to "provide monies with which to meet any municipal expense, the necessity or extent of which could not have been foreseen or reasonably evaluated at the time of adopting the annual budget." State law sets the maximum balance in the fund at \$.375 per \$1,000 of assessed valuation. This reserve would be used to address unforeseen expenditures (as opposed to revenue shortfalls addressed by the Revenue Stabilization Reserve). The fund can be replenished through interest earnings up to the maximum balance or through the year-end transfer if needed.

Reserves are an important indicator of the City's fiscal health. They effectively represent "savings accounts" that are established to meet unforeseen budgetary needs (general purpose reserves) or are otherwise dedicated to a specific purpose (special purpose reserves). The City's reserves are listed with their revised estimated balances at the end of the biennium in the table below:

General Government & Utility Reserves Summary

Reserves	2009-10 Est End Balance	2009 Auth. Uses	2009 Auth. Additions	Revised 2009-10 End Balance
GENERAL PURPOSE RESERVES				
Contingency	2,324,515			2,324,515
General Capital Contingency	2,444,561			2,444,561
Park & Municipal Reserve:				
General Oper. Reserve (Rainy Day)	2,712,836			2,712,836
Revenue Stabilization Reserve	1,082,380			1,082,380
Building & Property Reserve	2,059,669			2,059,669
Council Special Projects Reserve	271,960	51,000		220,960
Total General Purpose Reserves	10,895,921	51,000	0	10,844,921
SPECIAL PURPOSE RESERVES				
Excise Tax Capital Improvement:				
REET 1	8,370,417			8,370,417
REET 2	8,134,095			8,134,095
Equipment Rental:				
Vehicle Reserve	6,421,787			6,421,787
Radio Reserve	36,000			36,000
Information Technology:				
PC Replacement Reserve	494,373			494,373
Major Systems Replacement Reserve	247,900			247,900
Facilities Maintenance:				
Operating Reserve	550,000			550,000
Facilities Sinking Fund	1,051,963			1,051,963
Impact Fees				
Roads	3,429,578			3,429,578
Parks	237,809			237,809
Park Bond Reserve	558,981			558,981
Cemetery Improvement	523,405			523,405
Off-Street Parking	204,410			204,410
Tour Dock	70,175			70,175
Street Improvement	994,576			994,576
Firefighter's Pension	1,591,986			1,591,986
Park & Municipal Reserve:				
Litigation Reserve	51,329			51,329
Labor Relations Reserve	67,183			67,183
Police Equipment Reserve	48,093			48,093
LEOFF 1 Police Reserve	612,029			612,029
Facilities Expansion Reserve	800,000			800,000
Development Services Reserve	457,331			457,331
Tree Ordinance	28,980			28,980
Donation Accounts	161,257			161,257
Revolving Accounts	86,175			86,175
Water/Sewer Operating Reserve	1,799,424			1,799,424
Water/Sewer Debt Service Reserve	826,759			826,759
Water/Sewer Capital Contingency	3,018,240	182,000		2,836,240
Water/Sewer Construction Reserve	9,444,066			9,444,066
Surface Water Operating Reserve	394,485			394,485
Surface Water Capital Contingency	617,690			617,690
Surface Water-Transp. Related Rsv	1,302,179			1,302,179
Surface Water Construction Reserve	3,186,434			3,186,434
Total Special Purpose Reserves	55,819,109	182,000	0	55,637,109
Grand Total	66,715,030	233,000	0	66,482,030

No Council Authorized Additions as of June 30, 2009.

Reserve Summary *continued***USES AND ADDITIONS HIGHLIGHTS****RESERVE AMOUNT DESCRIPTION****2009 Council Authorized Uses**

Council Special Projects Reserve	\$26,000	Funding for federal lobbyist services for 2009.
	\$25,000	Funding for Neighborhood Connections in 2010.
Water/Sewer Capital Contingency	\$54,000	Additional funding of \$54,000 for telemetry system upgrades at Supply Station #2 to coincide with a City-wide upgrade of telemetry panels at other water facility sites.
	\$128,000	Funding for the completion of the 2009 Water System Improvement Project.

2009 Council Authorized Additions

No Council Authorized Additions as of June 30, 2009

The summary above details all Council authorized uses and additions to each reserve through June 2009.

General Government & Utility Reserves Targets Summary

Reserves	Revised 2009-10 End Balance	2009-10 Target	Over (Under) Target
GENERAL PURPOSE RESERVES			
Contingency	2,324,515	4,915,571	(2,591,056)
General Capital Contingency	2,444,561	9,032,430	(6,587,869)
Park & Municipal Reserve:			
General Oper. Reserve (Rainy Day)	2,712,836	3,567,649	(854,813)
Revenue Stabilization Reserve	1,082,380	2,188,803	(1,106,423)
Council Special Projects Reserve	220,960	250,000	(29,040)
General Purpose Reserves with Targets	8,785,252	19,954,453	(11,169,201)
SPECIAL PURPOSE RESERVES			
Excise Tax Capital Improvement:			
REET 1	8,370,417	1,653,500	6,716,917
REET 2	8,134,095	8,477,130	(343,035)
Firefighter's Pension	1,591,986	1,103,000	488,986
Park & Municipal Reserve:			
Litigation Reserve	51,329	50,000	1,329
Water/Sewer Operating Reserve	1,799,424	1,799,424	0
Water/Sewer Debt Service Reserve	826,759	826,759	0
Water/Sewer Capital Contingency	2,836,240	3,018,240	(182,000)
Surface Water Operating Reserve	394,485	394,485	0
Surface Water Capital Contingency	617,690	617,690	0
Special Purpose Reserves with Targets	24,622,425	17,940,228	6,682,197
Reserves without Targets	33,074,353	n/a	n/a
Total Reserves	66,482,030	n/a	n/a

An additional transfer of \$1 million from the Revenue Stabilization Reserve was approved with mid-year budget adjustments, which will effectively use up this reserve as a resource.

The table to the left compares the revised ending balance to the targets established in the budget process for those reserves with targets.



123 5th Avenue
Kirkland, Washington 98033
425-587-3101

- ◆ Tracey Dunlap, Director of Finance & Administration
- ◆ Michael Olson, Deputy Director of Finance & Administration
- ◆ Sandi Hines, Financial Planning Manager
- ◆ Sri Krishnan, Senior Financial Analyst
- ◆ Neil Kruse, Budget Analyst

www.ci.kirkland.wa.us

For past reports, keyword search " " "
FMR

The Financial Management Report (FMR) is a high-level status report on the City's financial condition that is produced quarterly.

- It provides a **summary budget to actual comparison** for year-to-date revenues and expenditures for all operating funds. The report also compares this year's actual revenue and expenditure performance to the prior year.
- The **Sales Tax Revenue Analysis** report takes a closer look at the City's largest and most economically sensitive revenue source.
- **Economic environment** information provides a brief outlook at the key economic indicators for the Eastside and Kirkland such as office vacancies, residential housing prices/sales, development activity, inflation and unemployment.
- The **Investment Summary** report includes a brief market overview, a snapshot of the City's investment portfolio, and the City's year-to-date investment performance.
- The **Reserve Summary** report highlights the uses of and additions to the City's reserves in the current year as well as the projected ending reserve balance relative to each reserve's target amount.
-

Economic Environment Update References:

- *Northwest purchasing managers' optimism grows*, Puget Sound Business Journal, July 7, 2009
- Eric Pryne, *June home sales are highest in King County since Oct. 2007*, The Seattle Times, July 7, 2009
- Tali Arbel, *Economic indicators up more than expected in June*, The Seattle Times, July 20, 2009
- *Washington state executives' confidence in economy reaches it lowest mark in nearly a decade*, Puget Sound Business Journal, July 24, 2009
- *U.S. House Prices keep Climbing With a 1.2% Rise in June*, Integrated Asset Services, August 11, 2009
- Washington State Economic and Revenue Forecast, Economic and Revenue Forecast Council, June 2009
- CB Richard Ellis Real Estate Services, Market View Puget Sound, Second Quarter 2009
- Washington State Employment Security Department
- Washington State Department of Revenue
- Washington State Department of Labor & Industries
- U.S. Bureau of Labor Statistics
- City of Kirkland Building Division
- City of Kirkland Finance Department

Additional reference:

- *Kirkland selected as Eastside venue for 2009 SIFF Film Festival*, PNWLocalNews.com, March 20, 2009